



THE CHAIRMAN

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

March 12, 2001

The Honorable John D. Dingell  
Ranking Member  
Committee on Energy and Commerce  
2322 Rayburn House Office Building  
U.S. House of Representatives  
Washington, DC 20515-6115

Dear Congressman Dingell:

I am pleased to respond to your letter dated January 29, 2001 to former Chairman Levitt. In your letter, you reference the Commission's most recent annual progress report to the Commerce Committee regarding regulatory and industry initiatives to improve corporate bond transparency. Your letter seeks additional information regarding these initiatives, requests information regarding alternative trading systems, and inquires about the status of the New York Stock Exchange's bond trading facility. As the issues you raise fall directly within the Division of Market Regulation's area of responsibility, at my request, the Division of Market Regulation has responded to your inquiries in the attached memorandum.

I appreciate your interest in corporate bond transparency. Please do not hesitate to contact me or Annette Nazareth, Director of the Division of Market Regulation, at (202) 942-0090, if you have further questions.

Sincerely,


A handwritten signature in cursive script, reading "Laura S. Unger".

Laura S. Unger  
Acting Chairman

Attachment

## MEMORANDUM

**TO:** Acting Chairman Unger

**FROM:** Annette L. Nazareth   
Division of Market Regulation

**DATE:** March 2, 2001

**RE:** Response to Congressman John D. Dingell's Inquiries Concerning  
Corporate Bond Transparency, Alternative Trading Systems, and the  
NYSE's Bond Trading Facility

In a letter dated January 29, 2001 to former Chairman Levitt, Congressman John D. Dingell requested certain information regarding: (i) regulatory and industry initiatives to improve corporate bond transparency; (ii) alternative trading systems that facilitate trading in debt securities; and (iii) reports in the press that the New York Stock Exchange is seeking to get out of the bond trading business. The following is in response to your request that the Division of Market Regulation address the questions raised in Congressman Dingell's letter.

### **I. Corporate Bond Transparency**

As you are aware, last month the Commission approved proposed rules by the National Association of Securities Dealers, Inc. ("NASD") that will greatly enhance price transparency in the corporate bond market. The new rules require NASD members to report transactions in most U.S. corporate bonds to the NASD. The rules also establish a facility, called TRACE, for collecting and distributing that information to the public. The Commission's approval of the TRACE Rules is a significant step towards improving bond market transparency.

Congressman Dingell's letter references Corporate Trades I, a corporate bond transaction reporting system established by The Bond Market Association in the spring of 1999. Corporate Trades I has had, and continues to have, a relatively narrow scope. It covers only transactions in investment grade bonds effected through interdealer brokers. Additionally, Corporate Trades I provides price information on a daily basis, and not in real time. In contrast, the TRACE Rules (which The Bond Market Association commented upon and supported during the proposing stage) apply to most investment grade and non-investment grade corporate bond transactions involving an NASD member. Moreover, during the first three months after implementation, the TRACE Rules provide for the NASD to make transaction information on investment grade bonds

with initial issuances of \$1 billion and above, and high-yield bonds in the current "FIPS-50" program, available on an immediate basis. Our expectation is that increased public availability of information about bond prices on a real-time basis will encourage greater participation in the corporate bond markets by brokers, dealers, and investors and thereby contribute to deeper, more competitive markets.

## II. Alternative Trading Systems that Trade Debt Securities

Congressman Dingell's letter requested certain information regarding alternative trading systems ("ATSs") that trade debt securities. In the past year, the number of systems that trade such securities has increased dramatically. As Congressman Dingell's letter indicates, The Bond Market Association has identified approximately 80 such systems. By contrast, as more fully explained below, only 36 such systems have filed reports with the Commission under Regulation ATS. We believe that the disparity between the 80 systems identified by The Bond Market Association and the 36 systems that have filed with the Commission is due to the fact that not all systems that facilitate trading in debt securities are subject to Regulation ATS. Specifically, any system that does not meet the definition of "exchange" under the Securities Exchange Act of 1934 is not subject to Regulation ATS. As such, systems identified by The Bond Market Association that display the quotes of and provide for execution by a single dealer, or that offer electronic order routing without providing an execution feature, are not subject to Regulation ATS. Additionally, systems identified by The Bond Market Association that limit their trading to certain securities regulated by the Department of Treasury (i.e., U.S. government securities and/or repurchase and reverse repurchase agreements on U.S. government securities) are also excluded from Regulation ATS. See discussion contained in Commission adopting release for Regulation ATS, Securities Exchange Act Release No. 40760 (December 8, 1998), 63 FR 70844, at 70852-70854, 70859-70861 (December 22, 1998).

Every electronic trading system to which Regulation ATS applies is required to register as a broker-dealer, become a member of a self-regulatory organization, make and keep records necessary to create a meaningful audit trail, and file reports with the Commission on Forms ATS and ATS-R. These reports contain information describing, among other things, how the ATS will operate (e.g., how pricing and execution occur), who may access it, and what types of securities it will trade. In addition, after the ATS has commenced operations, it is required to report quarterly total unit and dollar volume of transactions in different categories of securities. As members of the NASD, all of the broker-dealers that currently operate ATSs will be subject to the TRACE reporting requirements.

The information reported on Form ATS and Form ATS-R is reviewed by my staff. Section 301(b)(2)(vii) of Regulation ATS specifies that "all reports filed [thereunder] shall be deemed confidential when filed." As such, specific details regarding the operation of any particular ATS are not publicly available from the Commission. In response to Congressman Dingell's inquiry regarding ATS access and types of securities traded, I have asked my staff to compile that information and --

consistent with our duty of confidentiality -- provide it on a name-withheld basis. As the attached exhibit indicates, my staff has identified 25 ATSs currently available to trade debt securities. Of these, the top five systems reported approximately \$11.3 billion aggregate volume for transactions in corporate debt securities for the fourth quarter of 2000. An additional 11 systems have filed Form ATS, but are not currently operational.

### **III. Press Reports Regarding the New York Stock Exchange's Bond Trading Facility**

Congressman Dingell's letter cites an article in TheWall Street Journal stating that the New York Stock Exchange ("NYSE" or "Exchange") is seeking to "get out of the bond trading business." The Wall Street Journal, Friday, December 8, 2000, at C13.

This statement refers to the NYSE's Automated Bond System ("ABS"). ABS is an automated trading and information system that allows subscribing firms to enter and execute bond orders through terminals in their offices. ABS displays last-sale and bid/ask quotation data for NYSE-listed convertible and non-convertible bonds.

The NYSE has indicated that it intends to discontinue its ABS business because it has not been a significant growth area for the Exchange. These plans are currently on hold, however. If the NYSE sells or otherwise discontinues its ABS business, we do not believe that there will be a significant effect on corporate bond transparency, as many of the bonds traded on ABS will trade over-the-counter in the absence of ABS and thereby become subject to reporting through TRACE.

Attachment

